No. 88-1249 and 88-1250

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In the Supreme Court of the United States

OCTOBER TERM, 1988

SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY, ET AL., PETITIONERS

v.

FEDERAL COMMUNICATIONS COMMISSION, ET AL.

NEW ENGLAND TELEPHONE AND TELEGRAPH COMPANY, ET AL., PETITIONERS

v.

FEDERAL COMMUNICATIONS COMMISSION, ET AL.

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENTS IN OPPOSITION

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QUESTION PRESENTED

Whether the Commission has authority under the Communications Act of 1934, 47 U.S.C. 151 *et seq.*, to enforce its 1976 prescription of a rate of return for 1978 rates by requiring carriers to refund, through prospective rate reductions, revenues collected in 1978 in excess of the maximum prescribed return.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	14
Conclusion	30

TABLE OF AUTHORITIES

Cases:

Arizona Grocery Co. v. *Atchison, Topeka & Santa Fe R.R.*, 284 U.S. 370 (1932) 8, 16
AT & T v. *FCC*, 487 F.2d 865 (2d Cir. 1973) 2
AT & T, 57 F.C.C.2d 960 (1976) 4, 6
AT & T, 58 F.C.C.2d 1 (1976) 5, 6, 24, 25
AT & T, 38 F.C.C.2d 213 (1972) 6
AT & T, 86 F.C.C.2d 221 (1981) aff'd, 707 F.2d 610 (D.C. Cir. 1983) 22
Bebchick v. *PUC*, 313 F.2d 187 (D.C. Cir.), cert. denied, 373 U.S. 913 (1963) 25
Capital Cities Cable, Inc. v. *Crisp*, 467 U.S. 691 (1984) .. 3
City of New York v. *FCC*, 108 S. Ct. 1637 (1988) 3
FPC v. *Louisiana Power & Light Co.*, 406 U.S. 621 (1972) 3
FPC v. *Natural Gas Pipeline Co.*, 315 U.S. 575 (1942) ... 16
FPC v. *Tennessee Gas Transmission Co.*, 371 U.S. 145 (1962) 4, 18, 21, 25
FPC v. *Texaco, Inc.*, 417 U.S. 380 (1974) 17
General Telephone Co. v. *United States*, 449 F.2d 846 (5th Cir. 1971) 18
ICC v. *Brotherhood of Locomotive Engineers*, 107 S. Ct. 2360 (1987) 27-28
Las Cruces TV Cable v. *FCC*, 645 F.2d 1041 (D.C. Cir. 1981) 9
Massachusetts Trustees v. *United States*, 377 U.S. 235 (1964) 28
Nader v. *FCC*, 520 F.2d 182 (D.C. Cir. 1975) ..... *passim*

Cases—Continued: Page

North American Telecomm. Ass'n v. *FCC*, 772 F.2d 1282 (7th Cir. 1985) 3, 17
Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 2, 3, 16, 17, 18
SEC v. *Chenery Corp.*, 332 U.S. 194 (1947) 27, 28
United States v. *FCC*, 707 F.2d 610 (D.C. Cir. 1983) 4, 22
Wisconsin v. *FPC*, 373 U.S. 294 (1963) 18-19

Statutes:

Communications Act of 1934, 47 U.S. 151 *et seq.* 2
§ 4(i), 47 U.S.C. 154(i) ..... *passim*
§ 201(b), 47 U.S.C. 201(b) 2
§ 202(a), 47 U.S.C. 202(a) 2
§ 203, 47 U.S.C. 203 ..... 17, 20
§ 204, 47 U.S.C. 204 ..... *passim*
§ 204(a), 47 U.S.C. 204(a) 3, 24
§ 205, 47 U.S.C. 205 ..... *passim*
§ 205(a), 47 U.S.C. 205(a) 2, 16
§ 206, 47 U.S.C. 206 18
§§ 206-209, 47 U.S.C. 206-209 ..... 12, 22
§ 209, 47 U.S.C. 209 18
§ 408, 47 U.S.C. 408 ..... 2, 16
Natural Gas Act, 15 U.S.C. 717 *et seq.*
15 U.S.C. 717*o* 3
15 U.S.C. 717d(a) 16
41 Stat. 488-491 22-23

Miscellaneous:

Authorized Rates of Return for the Interstate Services of AT&T Communications and Exchange Telephone Carriers (CC Docket No. 84-800 Phase III), FCC 86-354 (released Aug. 25, 1986) 22
FCC News Rep. No. DC-1379, *Commission Adopts Incentive Regulation for Dominant Carriers* (Mar. 16, 1989) 28
P. Garfield & W. Lovejoy, *Public Utility Economics* (1964) 4

Miscellaneous – Continued: Page

H.R. Rep. No. 193, 73d Cong., 1st Sess. (1933) 23

Inquiry Concerning AT&T's Earnings on Interstate and Foreign Services During 1978, 75 F.C.C.2d 412 (1979) 6, 7, 26

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-39a)[1] is reported at 826 F.2d 1101. The initial order of the Federal Communications Commission (Pet. App. 40a-72a) is reported at 102 F.C.C.2d 52. The Commission orders denying reconsideration (Pet. App. 86a-120a, 121a-129a) are not reported.

JURISDICTION

The judgment of the court of appeals (Pet. App. 130a-132a) was entered on August 21, 1987. A petition for

[1] "Pet. App." refers to the appendix to the petition for a writ of certiorari in No. 88-1250.

rehearing was denied on November 2, 1988. Pet. App. 133a-140a. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Under the Communications Act of 1934, 47 U.S.C. 151 *et seq.* (Act), the Federal Communications Commission (FCC or Commission) is responsible for ensuring that the regulations, classifications, charges, and practices of carriers of interstate and foreign communications are just, reasonable, and non-discriminatory. 47 U.S.C. 201(b), 202(a). The Act provides the Commission with a number of regulatory tools to carry out that broadly defined responsibility. In particular, under Section 205, the Commission may investigate a carrier's rates and practices; and if, after a hearing, it finds that a rate or practice is or will be unlawful under the Act, the Commission may prescribe just and reasonable rates or practices "to be thereafter observed." 47 U.S.C. 205(a). Such a prescription is binding on the carrier, which "shall not thereafter publish, demand, or collect any charge other than the charge so prescribed, or in excess of the maximum * * * so prescribed * * * and shall conform to and observe the regulation or practice so prescribed." *Ibid.* Any such prescription is binding for the time specified in the Commission's order or until the order is superseded. 47 U.S.C. 408. See *Permian Basin Area Rate Cases,* 390 U.S. 747, 779 (1968) (no "limitations of time" imposed by statute on agency prescription order); *AT & T* v. *FCC,* 487 F.2d 865, 880 (2d Cir. 1973).

The Commission has additional powers to investigate the lawfulness of proposed new practices or charges under Section 204 of the Act. It may suspend the effectiveness of such practices or rates for up to five months pending its investigation. In the case (as is involved here) of a proposed

increased rate, if the investigation is not completed after the specified period of suspension, the Commission may allow the rate to take effect but require the carrier to keep an accounting of the amounts it collects under the rate. At the end of the investigation, the Commission may order the carrier "to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such charge * * * as * * * shall be found not justified." 47 U.S.C. 204(a).

Supplementing those and other express provisions of the Act, Section 4(i) authorizes the agency to "perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this chapter, as may be necessary in the execution of its functions." 47 U.S.C. 154(i). That provision is a "necessary and proper clause." *North American Telecomm. Ass'n* v. *FCC*, 772 F.2d 1282, 1292 (7th Cir. 1985). It gives the FCC a flexible and wide-ranging power to take steps to implement Congress' broadly worded directives defining the Commission's rate regulation and other responsibilities.[2]

In 1972, the Commission, under its Section 4(i) authority to take necessary and proper measures to implement its Section 205 power to prescribe just and reasonable rates and practices, asserted the authority to prescribe the rate of return a carrier may earn. See Pet.

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[2] See, *e.g.*, *City of New York* v. *FCC*, 108 S. Ct. 1637, 1643 (1988); *Capital Cities Cable, Inc.* v. *Crisp*, 467 U.S. 691, 700 (1984); *North American Telecomm. Ass'n* v. *FCC*, 772 F.2d at 1292-1293. Cf. *FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621, 642 (1972) (Natural Gas Act, 15 U.S.C. 717*o*) ("the Commission must possess broad powers to devise effective means to meet these responsibilities"); *Permian Basin Area Rate Cases*, 390 U.S. 747, 774-777 & n.40 (1968) (same).

App. 4a-5a.[3] That authority was upheld by the D.C. Circuit and has not been questioned elsewhere. *Nader* v. *FCC,* 520 F.2d 182, 203-204 (D.C. Cir. 1975). See *United States* v. *FCC,* 707 F.2d 610 (D.C. Cir. 1983). The D.C. Circuit ruled that such rate of return prescriptions are "necessary for the Commission to carry out its [ratemaking] functions in an expeditious manner." *Nader* v. *FCC,* 520 F.2d at 204. Cf. *FPC* v. *Tennessee Gas Transmission Co.,* 371 U.S. 145, 150-155 (1962) (upholding FPC's order of refund based on determination of the reasonable rate of return, prior to any determination of how the costs of service should be allocated). The court also explained that a rate of return prescription, like any other Section 205 prescription, is binding: it limits the utility prospectively to the prescribed return. *Nader* v. *FCC,* 520 F.2d at 201. The court further pointed out that, although such a prescription protects the carrier from "the possibility of refunds on the ground that [the] * * * [prescribed] return [i]s too high, the Commission retains full latitude to order refunds on all other grounds." *Id.* at 205 n.25.

2. a. This case involves the FCC's enforcement of a rate of return prescription. In 1976, after a lengthy hearing, the Commission prescribed a rate of return of 9.5 percent for AT & T and its then-affiliated operating companies. *AT & T,* 57 F.C.C.2d 960 (Feb. 5, 1976). Although 9.5

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[3] The rate of return is one of the components of the formula that is typically used to determine the revenue requirements, and hence the rates, of a regulated company. The rate of return may be defined as "the amount of money a utility earns, over and above operating expenses, depreciation expense, and taxes, expressed as a percentage of the legally established net valuation of utility property, the rate base." P. Garfield & W. Lovejoy, *Public Utility Economics* 116 (1964). Under one common form of rate regulation, a regulated carrier is authorized to set rates that will recover its legitimate expenses (including depreciation and taxes) plus a reasonable return (the rate of return) on its rate base (the net investment of property).

percent was the prescribed return, the Commission afforded the company a .5 percent margin of error, specifying that "AT&T should be permitted 'a level or range of interstate earnings not to exceed 10%' " and that the Commission would not require "any downward adjustment of AT&T's overall interstate rates provided its overall rate of return does not exceed 10 percent." *Id.* at 973.

AT & T filed rates that it stated were designed to achieve the prescribed rate of return of 9.5 percent. Without finding that the rates were just and reasonable, the Commission, exercising its Section 204 power, suspended the rates for one day and then permitted them to go into effect on February 29, 1976, subject to an accounting order for possible refund. *AT & T*, 58 F.C.C.2d 1, 4 (Feb. 26, 1976).[4] AT & T was required to keep an accounting, not customer-by-customer, but "by service classes and subclasses, in the aggregate." *Id.* at 5.

In requiring the accounting and retaining the power to compel a refund, the Commission stated that its recent prescription of the rate of return had left unresolved "numerous other issues * * * which control the individual rates which AT & T may charge for specific services and the expenses and rate base upon which the rate of return is calculated." 58 F.C.C.2d at 4. The Commission expressly listed other components of a full determination of a just and reasonable rate—the correctness and legitimacy of AT & T's claimed investments, cash expenses, and non-cash expenses such as depreciation, and whether "the rates proposed or in effect actually * * * produce a fair rate of return." *Ibid.* (quoting *Nader* v. *FCC,* 520 F.2d at 204). Of course, without resolving those issues, it was not possible to determine whether the actual rates charged by AT & T

[4] The Commission limited the suspension to a single day in order to avoid subverting AT & T's "opportunity to earn the fair rate of return which we have prescribed." 58 F.C.C.2d at 4.

would produce the rate of return that the Commission prescribed.[5]

b. After the rates had become effective and had been collected for almost three years, the data contained in monthly reports that AT & T filed with the Commission indicated that AT & T's earnings in 1978 had exceeded not only the authorized return of 9.5 percent but also the established buffer of an additional .5 percent. Accordingly, in October 1979, the Commission issued a notice of inquiry to determine what action it should take in response to the apparent violation of its rate of return prescription. *Inquiry Concerning AT&T's Earnings on Interstate and Foreign Services During 1978,* 75 F.C.C.2d 412 (1979).[6] In requesting comments on what action it should take, including comments on the option of ordering a refund, the notice of inquiry twice pointed to the suspension and accounting order that allowed the 1978 rates to take effect (*id.* at 414 n.5, 415 n.6) and stated that the notice was

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[5] Petitioners fail to mention that the 1978 rates (filed in 1976) took effect subject to an accounting order. Petitioners in No. 88-1249 state that "there was no relevant accounting order." 88-1249 Pet. 6. Petitioners in No. 88-1250 state that AT & T "filed rates * * * and the FCC allowed them to become effective" (88-1250 Pet. 6); they also state that "[n]o suspension, investigation and accounting order was entered in connection with Bell's rate of return when it filed its rates in 1976" (*id.* at 14 n.19).

[6] The 1976 rate of return prescription of 9.5 percent was in effect for five years. During that time, AT & T's overall rate of return was 9.69 percent. Moreover, in four of the five years—all of the years in which the prescription was in effect for all 12 months—AT & T's rate of return exceeded 9.5 percent. Pet. App. 14a-15a. In 1976, AT & T's earnings were 9.25 percent; but its authorized rate of return during the first two months of that year was only 8.5 percent. *AT & T,* 38 F.C.C.2d 213, 245 (1972). The Commission's order prescribing a 9.5 percent rate of return was released on February 5, 1976, and the new rates implementing that prescription became effective on February 29. *AT & T,* 57 F.C.C.2d at 960; *AT & T,* 58 F.C.C.2d at 1, 4, 5.

issued pursuant to Sections 4(i), 204, and 205 of the Act (among others) (75 F.C.C.2d at 416).

c. After considering the comments filed by industry and consumer groups, the Commission determined that AT & T had earned a rate of return for its interstate and foreign services of 10.22 percent during 1978. Pet. App. 46a-51a. Noting that there were insuperable practical obstacles (especially after the AT & T divestiture) to distributing individually calculated refunds to each of the millions of AT & T's 1978 ratepayers, many of whom might no longer be in existence or identifiable, the Commission chose instead a class-wide refund mechanism consistent with the non-individualized accounting that it had required for the filing of the rates at issue: the Commission required downward adjustments of 1985 rates, to be apportioned among AT & T and the divested Bell Operating Companies (BOCs). *Id.* at 53a-54a. The Commission thus ordered AT & T and the BOCs to pay back the 1978 earnings in excess of a 10 percent rate of return by means of "a temporary discount upon interstate services for a period that is sufficient to reduce carrier revenues by the amount that is to be restored to interstate ratepayers." *Id.* at 52a.

The Commission rejected the suggestion that the 1976 rate of return prescription had not been intended to operate as a limit on AT & T's earnings. The Commission observed that the plain language of the prescription order had provided that AT & T's earnings were " 'not to exceed 10 percent.' " Pet. App. 56a. Relying on Section 205, the Commission noted that a "carrier is under an affirmative duty to revise its rates to conform to [an] outstanding prescription order." Pet. App. 58a. It further observed that "[t]he proper procedure for a carrier who contends that an outstanding order is improper is to petition the Commission to modify that order," which AT & T did not do. *Id.* at 56a-57a (footnote omitted).

The Commission also rejected the argument that it had accepted the rates when they were filed in 1976, that those rates had become lawful, and that the Commission could not later declare them unlawful. Pet. App. 57a-58a. The Commission pointed out that it had never found that the 1978 charges were just and reasonable and, indeed, had found some charges for particular services that were in effect in 1978 to be unlawful in other proceedings. *Id.* at 57a. It elaborated on that conclusion in a lengthy Appendix B to its decision (*id.* at 73a-85a), which noted that the rates in effect in 1978 had been suspended and subjected to an accounting order issued in reliance on Section 204 and Section 4(i) (Pet. App. 73a, 85a).

Finally, the Commission rejected the contention that it lacked authority to order a refund because Section 205 of the Communications Act did not specifically authorize refunds of revenues in excess of a prescribed rate of return. The Commission pointed simply to its Section 4(i) authority. It concluded that the court in *Nader* v. *FCC*, 520 F.2d at 204-205 & n.25, had recognized that "the power to order refunds is inherent in the Commission's prescription authority." Pet. App. 59a.

d. On reconsideration, the Commission reaffirmed its authority to adopt the restitution mechanism. See Pet. App. 101a-105a. The Commission rejected the contention that the order constituted retroactive ratemaking. *Id.* at 101a-104a. It noted that the restitution order "involved the enforcement of an outstanding order that was by its terms prospective" (*i.e.*, the 1976 rate of return prescription); and it pointed out again that it had never "authorized" the 1978 rates (*id.* at 102a n.55 (citing Appendix B of its initial order)). The Commission observed that *Arizona Grocery Co.* v. *Atchison, Topeka & Santa Fe R.R.*, 284 U.S. 370 (1932) (*Arizona Grocery*), and other ratemaking retroactivity decisions relied on by petitioners, involved "circumstances in which the regulatory body actually set the

specific price, or 'charge', that was to be paid by the user of the regulated entity's service"; here, by contrast, the Commission set the rate of return, not the rate, and the carrier itself set the charges subject to the constraints imposed by the rate of return prescription. Pet. App. 103a n.55, 103a-104a.

The Commission also reaffirmed its rejection of the argument that a rate of return prescription was not intended to be binding but merely to set a goal for future ratemaking. Pet. App. 104a-105a. The Commission cited a D.C. Circuit decision that had upheld a refund decision under Section 204 involving rates that, when filed, had not been found just and reasonable (*Las Cruces TV Cable* v. *FCC*, 645 F.2d 1041 (1981)) and again cited Appendix B of its initial decision, which showed that AT & T's 1978 rates were in a similar position. Pet. App. 104a n.60. The Commission also explained that the particular rate of return prescription order involved here clearly had restricted the amount that AT&T could earn on its interstate operations. While AT & T was required in the first instance to file rates "targeted" to earn 9.5 percent, the order set a "clearly stated upper bound" of 10 percent. *Id.* at 104a-105a. See also *id.* at 109a-111a (citing *Nader* v. *FCC* and FCC decisions since 1972, Commission rejects suggestion that treating rate of return prescription as setting upper bound was a new policy). Finally, the Commission reiterated that the restitution mechanism it chose was amply justified—in preference to a refund of excess charges to each individual 1978 customer—as "the least expensive, and most efficient, approach to effecting restitution." *Id.* at 111a-112a.[7] The Commission subsequently denied petitions seeking further reconsideration or clarification. *Id.* at 121a-129a.

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[7] The Commission noted its concern "that direct credits to each customer's bill would be more expensive than providing a

3. The court of appeals affirmed. Pet. App. 1a-20a. The court first ruled that a prescription of a rate of return does not merely require that carriers target their rates to try to achieve that return, as petitioners contended, but also declares that any higher return "is unlawful and *shall not occur.*" *Id.* at 9a. The court explained that petitioners' view of the Commission's Section 205 authority focused only "on carriers' subjective efforts, not on future events," and that the Commission's objective view is a more reasonable construction of the statute: "The Commission's chief concern in issuing prescriptions is protecting just and reasonable rates, not policing carriers' states of mind." Pet. App. 9a. Indeed, the court pointed out that, in *Nader* v. *FCC*, it had made clear that a rate of return prescription is no less binding than a rate prescription: the order at issue in *Nader* had " 'the prospective effect of a prescription, thus *limiting the utility to that return.*' *Nader, supra,* 520 F.2d at 202 (emphasis added)." Pet. App. 10a. Hence, while AT & T was required to target its rates to achieve the prescribed 9.5 percent rate of return, it was also forbidden actually to earn more than the 10 percent rate that included the .5 percent buffer, and was free to file adjusted rates as necessary to avoid that result.

Turning to the question of remedy, the court of appeals, after stating without explanation that Section 204 does not apply to this case, held that the Commission had the authority under Section 4(i) of the Communications Act to enforce its rate of return prescription by requiring the re-

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discount on future services," citing, among other things, comments that AT & T had filed. Pet. App. 112a & n.86.

The Commission pointed to the same set of practical difficulties in explaining why it chose the mechanism of a future rate reduction rather than basing a restitution plan on the complex series of service-by-service accounting orders for specific services described in Appendix B of the initial decision. Pet. App. 112a n.87.

fund of AT & T's excessive earnings. Pet. App. 10a-15a.[8] That provision, the court noted (*id.* at 12a), is a "wide-ranging source of authority" that expressly authorizes measures " 'necessary in the execution of [the Commission's] functions.' " Here, the court pointed out: "In a strictly technical sense, the Commission's choice of remedy was absolutely necessary; without the reductions, the carriers in fact would not be limited to a return of 10% and the prescription would be violated." *Ibid.* In any event, the court said, "the Commission enjoys significant discretion to choose among a range of reasonable remedies, including refunds." *Ibid.* While the Commission might have taken other corrective action, the court concluded (*ibid.*), "the measure it adopted in this case was appropriate and reasonable."

The court rejected the suggestion that the refund order constituted retroactive ratemaking. The court explained simply: "There was not retroactive ratemaking here, because the carriers' obligations were set prospectively in 1976, when the Commission forbade AT & T from earning more than 10%." Pet. App. 13a. In requiring refunds for 1978 earnings in excess of the prescribed return, the court added, the Commission's order "merely recognized that the prior prescription had been violated and imposed a remedy for the violation." *Ibid.* The court agreed with the observation of the Commission in its brief that " '[t]he carriers are being required merely to give up what they never should have collected in light of the rate of return prescription.' " *Ibid.*

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[8] The court pointed out that "the order does not impose a refund in the classic sense of restitution" because "the reductions will accrue to the benefit of a different customer base from the base that contributed to AT&T's excessive earnings." Pet. App. 11a. The court held, however, that even if the remedy were properly characterized as a refund, "the order was well within the agency's statutory authority." *Ibid.*

The court also ruled that the Commission's order did not distort the regulatory balance between the interests of ratepayers and carriers. Pet. App. 13a-15a. First, the court pointed out that the 1976 rate of return prescription provided a measure of protection to carriers, as it protected them against any subsequent claim for refund on the ground that the rate of return was too high. *Id.* at 13a-14a (quoting *Nader* v. *FCC*, 520 F.2d at 205 n.25). Hence, if AT & T's cost of capital in the market had plunged below the prescribed rate of return, so that AT & T could offer an above-market return to attract capital, the Commission could not have sought a refund on that ground, but would have had to initiate a new proceeding to set a new, prospectively applicable rate of return. *Id.* at 14a.

Second, the court observed that, although the Commission required refunds for excessive rates of return but had not provided for carriers to be compensated for shortfalls in the rate of return, that asymmetry was not improper: carriers "are entitled only to earn an overall reasonable return," and they have an ample opportunity to do so. Pet. App. 14a. Thus, the court noted that carriers may at any time file new rates that are designed to achieve an adequate return; if a shortfall appears likely, carriers can propose an appropriate rate change. *Id.* at 14a, 15a. Indeed, in this respect, the refund/shortfall asymmetry reflects a carrier/ratepayer asymmetry: while carriers may file rate changes to protect themselves against shortfalls, ratepayers, the court explained, must rely predominantly on the Commission to protect them from unlawful charges. *Id.* at 14a.[9] Moreover, the court noted that the .5 percent buffer both in general made it easier for carriers to design rates targeted to produce more than the 9.5 percent figure but less than the 10 percent ceiling and, in this case, "more

[9] Ratepayers may also seek damages in certain circumstances pursuant to Sections 206-209 of the Act, 47 U.S.C. 206-209.

than adequately protected" AT & T's interests; during three of the five years in which the 1976 prescription was in effect, "the carrier's rates were designed precisely enough to produce a return above the ceiling but not so far above as to trigger a Commission remedy." *Id.* at 14a-15a. See note 6, *supra*. In short, the court concluded that the Commission's order did not "foster an impermissible balance between the interests of the carriers and those of the consumers." *Id.* at 13a.

Finally, the court of appeals rejected several challenges that petitioners do not renew in their petitions in this Court. Pet. App. 15a-20a. In particular, the court rejected the contention that, even if the refund order was lawful, it represented an abrupt reversal of prior policy and therefore could not be applied in the present case. The court explained that the order, far from reversing a prior policy, simpy responded to a new situation: "never before had a carrier exceeded a rate-of-return prescription." *Id.* at 16a. In any event, petitioners clearly could show no detrimental reliance on the non-enforcement of the prescription, as they conceded—indeed, insisted—that "they made every effort to comply with the prescription." *Id.* at 17a. In addition, the court of appeals rejected several of petitioners' challenges to the Commission's method of computing the carriers' liability. *Id.* at 18a-20a.

Judge Buckley dissented. Pet. App. 20a-39a. He did not argue, however, that the court erred in upholding the Commission's statutory authority to order the refund; in his view, the issue of statutory authority should not have been addressed. *Id.* at 21a. Rather, Judge Buckley would have set aside the Commission's order on the ground (not presented by petitioners in this Court) that the refund policy could not be applied to petitioners in any event because it represented an abrupt alteration of prior Commission policy. *Ibid.*

4. After the Commission issued its refund order in this case, it promulgated a general rule requiring all carriers to refund earnings they receive in excess of a previously established rate of return. In a decision rendered after the decision in the present case, the court of appeals, while reaffirming the present decision, set aside the Commission's general refund rule as arbitrary and capricious and remanded to the Commission. Pet. App. 141a-161a. Subsequently, the full court of appeals denied en banc rehearing of both cases. *Id.* at 133a-140a, 160a-166a. Judge Starr, joined by Judges Buckley and Williams, would have granted en banc review on the ground that the Commission's position, in this case as well as in the general rulemaking case, is inconsistent with the statutory scheme. *Id.* at 135a, 162a; see *id.* at 152a-159a.

ARGUMENT

The decision of the court of appeals does not warrant this Court's review. First, the court correctly held that the Commission had authority under Section 4(i) to enforce its earlier rate of return prescription by directing the carriers to pay back their excess collections; and that ruling does not conflict with any decision of this Court or of any other court of appeals.[10] Second, the court's affirmance of the Commission's order is independently justified on another ground, though one not relied on by the court of appeals—that the order in this particular case was authorized under Section 204 (in combination with Section 4(i)) of the

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[10] The law in the D.C. Circuit is " 'distressingly unsettled' " (88-1250 Pet. 20, quoting Pet. App. 135a) only in the limited sense that three of the judges have expressed their disagreement with the position adopted by two panels of the circuit. That position, in upholding the refund order here, follows logically from the earlier decision in *Nader* v. *FCC*, 520 F.2d at 202-206, and is not in conflict with any other decision of the D.C. Circuit.

Communications Act. Third, the continuing importance of the issue decided in the case is uncertain; and if the issue recurs, it is more appropriately reviewed in another case—particularly, in the context of the general Commission rulemaking on the refund question, currently on remand from the court of appeals.

1. The court of appeals correctly held that the FCC acted within its Section 4(i) authority in requiring the petitioner carriers to refund, through a reduction in future rates, the revenues AT & T collected in 1978 in excess of the maximum rate of return prescribed in 1976. Rate of return prescriptions are statutorily authorized. And a refund is clearly justified as a necessary means of enforcing such prescriptions.

a. The Commission undoubtedly has the authority, under Section 4(i) in conjunction with Section 205, to prescribe rates of return for the communications carriers it regulates. Section 205 permits the Commission to prescribe just and reasonable "charges" and "practices," and Section 4(i) broadly authorizes the Commission to make rules and to issue orders that are "necessary in the execution of its functions." Prescribing a rate of return allows the Commission to settle one of the critical issues that determine the lawfulness of particular rates, freeing both carriers and the Commission to focus on the other issues, such as the validity of elements of the rate base and of particular expenses. Accordingly, the D.C. Circuit expressly affirmed the Commission's authority to prescribe rates of return in 1975, *Nader* v. *FCC*, 520 F.2d at 203-206, explaining that such prescriptions are "necessary for the Commission to carry out its [ratemaking] functions in an expeditious manner" (*id.* at 204). Such authority is well within the broad authority that this Court has frequently recognized that ratemaking agencies have " 'to make the pragmatic adjustments which may be called for

by particular circumstances.' " *Permian Basin Area Rate Cases*, 390 U.S. at 776-777 (quoting *FPC* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 586 (1942)). Such authority has been well established since 1975, and, indeed, petitioners do not openly challenge it here.

Any prescription issued under Section 205 has binding, coercive effect. Section 205 declares that a "charge" or "practice" prescribed under that provision is "to be thereafter observed"; and it further states that carriers "shall not thereafter publish, demand, or collect any charge other than the charge so prescribed, or in excess of the maximum * * * so precribed * * * and shall conform to and observe the regulation or practice so prescribed." 47 U.S.C. 205(a).[11] Prior to the 1976 prescription at issue here, moreover, *Nader* v. *FCC* made clear that a rate of return prescription had the binding effect of limiting the carrier to the prescribed rate of return (plus the buffer). 520 F.2d at 201-202. The 1976 prescription itself stated that AT & T's rate of return was " 'not to exceed' " the 10 percent enforcement-triggering ceiling. Pet. App. 6a. Hence, the court of appeals correctly held that the 1976 rate of return prescription was "no less binding" than a prescription of rates and had the " 'the force of a statute. . . . The carrier [was] bound to conform.' " *Id.* at 10a (quoting *Arizona Grocery*, 284 U.S. at 386).

An inherent and necessary corollary of the power to adopt binding rate of return prescriptions is the authority to enforce those prescriptions. This Court has often recog-

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[11] An order remains binding until superseded. See 47 U.S.C. 408 (FCC orders "shall continue in force for the period of time specified in the order or until the Commission or a court of competent jurisdiction issues a superseding order"). Cf. *Permian Basin Area Rate Cases*, 390 U.S. at 779 ("Nothing in [15 U.S.C. 717d(a)] imposes limitations of time upon the effectiveness of rate determinations issued under it; rather, the section provides that rates held to be just and reasonable are 'to be thereafter observed * * *.' ").

nized in the ratemaking context that " 'the width of administrative authority must be measured in part by the purposes for which it was conferred * * *.' " *FPC* v. *Texaco, Inc.*, 417 U.S. 380, 389 (1974), quoting *Permian Basin Area Rate Cases,* 390 U.S. at 776. Section 4(i), which serves as a "necessary and proper" clause (*North American Telecomm. Ass'n* v. *FCC*, 772 F.2d at 1292-1293), is by its terms designed to provide flexibility to the Commission in carrying out its statutory responsibilities. The enforcement of a prescription that is authorized under Section 205 is at the core of the enforcement authority that Section 4(i) grants the Commission. Again, petitioners do not expressly dispute that the Commission must be able to enforce its prescriptions.

As the court of appeals recognized, once the validity of rate of return prescriptions and the Commission's authority to enforce such prescriptions are accepted, the power to require refunds is readily justified as a tool to enforce a rate of return prescription. A refund is the most obvious means of ensuring that a directive establishing a maximum rate of return is not violated; indeed, a backward-looking remedial mechanism such as a refund is unavoidable where the prescription at issue is of a rate of return, because not until revenues are actually collected can it be determined whether the carrier actually exceeded the prescribed rate of return.[12] Thus, the court of appeals in

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[12] If the rates themselves are prescribed, a refund mechanism is necessary if the carrier actually charges in excess of the prescribed rates. Pet. App. 13a. Similarly, if the rates are allowed to go into effect but not found lawful by the Commission in advance, then a refund may be a necessary means of enforcing a subsequent determination of lawful rates. See 47 U.S.C. 204 (expressly authorizing refunds). If a carrier in fact charges the rates found lawful and prescribed by the Commission in advance, then there is no inherent justification for a backward-looking review of actual collections. Accordingly, because carriers' rates must be published and adhered to (47 U.S.C. 203), the

this case stated that the Commission's choice of the refund remedy, in "a strictly technical sense," was "absolutely necessary," because otherwise "the carriers in fact would not be limited to a return of 10% and the prescription would be violated." Pet. App. 12a.[13]

In any event, the FCC "enjoys significant discretion to choose among a range of reasonable remedies." Pet. App. 12a; *Nader* v. *FCC*, 520 F.2d at 203; see *General Telephone Co.* v. *United States*, 449 F.2d 846, 865 (5th Cir. 1971) (courts "must give deference to the choice of remedy selected by the agency," which should be upheld if it is "reasonably calculated to effectuate the policies of the Communications Act"). Refunds are well within that range. Indeed, compensatory remedies are expressly provided for in other sections of the Communications Act, 47 U.S.C. 204, 206, 209, and a refund is a well-established remedial device in utility regulation generally. See, *e.g.*, *Permian Basin Area Rate Cases*, 390 U.S. at 825-828; *FPC* v. *Tennessee Gas Transmission Co.*, 371 U.S. at 150-155.[14]

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issue of refunds, outside the Section 204 context, became significant only after the Commission began in 1972 to prescribe carriers' rates of return rather than only their rates.

[13] Petitioners in No. 88-1249 (at 11 n.15) state that the Commission's remedy "was to order that the rates on file be retargeted to the prescribed return." That argument ignores the fact that the Commission already had issued an order—the rate of return prescription—that had been violated. Nothing in the statutory scheme supports the suggestion that the only enforcement tool for violation of an agency order is to issue another order that may itself be violated.

[14] It would be inconsistent with the longstanding approach to the interpretation of the broadly worded ratemaking statutes—indeed, it would stand that approach on its head—to suggest that the Commission, when choosing a means of enforcing a form of order that is authorized by, though not specifically mentioned, in the statute, is forbidden to adopt remedies that are specifically provided for elsewhere in the statute. Cf. *Wisconsin* v. *FPC*, 373 U.S. 294, 309

b. Contrary to petitioners' contention, the requirement that they refund earnings in excess of the prescribed maximum return in no way violates the rule against retroactive ratemaking. The reason is simple: as the court of appeals explained, there was no retroactive ratemaking here, because the obligation being enforced was set prospectively in 1976 when the FCC issued its rate of return prescription. Pet. App. 13a. The refund order merely imposed a remedy for the carriers' violation in 1978 of the duty that was imposed in 1976. *Ibid.*

For that reason, petitioners' assertion that the decision below conflicts with numerous decisions concerning retroactive ratemaking is incorrect. See 88-1249 Pet. 13-18; 88-1250 Pet. 11-16. None of those decisions involved the situation that is at issue in this case—agency action enforcing an existing, prospectively defined prescription, let alone a rate of return prescription. Nothing in those decisions forbids a ratemaking agency's use of a refund to enforce, in a practical, administratively convenient manner, a valid, prospective agency order.[15]

Similarly, the Commission's choice of remedy to enforce its rate of return prescription does not disturb the balance between the interests of carriers and customers that Congress has established in the Communications Act. Of course, the Commission order must be judged on the basis of the provisions of the statute, not on the basis of an

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(1963) ("to declare that a particular method of rate regulation is so sanctified as to make it highly unlikely that any other method could be sustained would be wholly out of keeping with this Court's consistent and clearly articulated approach to the question of the Commission's power to regulate rates").

[15] The prospective nature of the FCC's action here is underscored by the fact that it did not order refunds by the independent (*i.e.*, non-AT & T) telephone companies, because the agency had not prescribed a rate of return limitation for those companies. Pet. App. 117a-118a & n.108.

idealized structure that imposes one particular vision of alleged "symmetry" that is not expressed in the statute itself. As we have shown, the refund order is authorized by the statute. In any event, as the court of appeals concluded, the Commission's order properly respects the statutory balance of carrier and ratepayer protection. Pet. App. 15a.

First, the Commission permitted AT & T a margin of .5 percent above the prescribed just and reasonable level of 9.5 percent, recognizing the imprecision of ratemaking and providing the carriers an incentive for efficiency. Only when—and to the extent that—AT & T exceeded both the 9.5 percent prescription and the .5 percent margin did the Commission require a refund. AT & T thus had ample room to set rates that were designed to achieve the authorized rate of return without fear of refunds caused by minor forecasting errors.[16]

Second, AT & T had an adequate opportunity to seek relief from anticipated shortfalls. If it appeared likely that the rates established by AT & T would be inadequate to achieve the prescribed return, AT & T could have filed tariff revisions. See 47 U.S.C. 203. On a proper showing, the Commission would have allowed such revisions to become effective promptly. As the court of appeals noted, AT & T presumably had every incentive to seek such revisions. Pet. App. 18a. And the Commission, having set a

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[16] In the general rulemaking proceeding, the court of appeals invalidated the Commission's general refund rule, explaining that the present case was different because here the Commission provided " 'ample protection for the carriers' interests.' " Pet. App. 149a-151a. The court also observed that the validity of the refund rule depended critically on whether the buffer was large enough so that expected swings in earnings deviated from the authorized rate of return by no more than that amount. *Id.* at 147a n.4. For AT & T during 1976-1980, of course, that was so, with the exception of 1978.

fair rate of return, reasonably could rely on AT & T to protect itself against a shortfall.[17]

Third, AT & T was always protected against the possibility that the Commission would order a refund on the ground that the prescribed rate of return was too high. Thus, if the cost of capital had fallen in 1977—after the FCC's prescription order had become effective—so that AT & T's achieved return of 9.59 percent in that year had been far above a level reasonably necessary to attract investment, the Commission would have been foreclosed by its prescription order from requiring a refund on that basis. Pet. App. 13a-14a (citing *Nader* v. *FCC*, 520 F.2d at 205 n.25). The Commission would have had to initiate and to complete a proceeding to revise its prescription order prospectively to eliminate that protection from AT & T

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[17] The record in this case does not support a finding that AT & T failed to achieve its authorized rate of return during any period of time in which the prescription was in effect. During the five years in which the 9.5 percent prescription was in effect, AT & T's rate of return averaged 9.69 percent—well above the prescribed level. Pet. App. 14a. Petitioners allege that there was a shortfall in 1976, but their sole support for that contention is that AT & T's earnings in that year were 9.25 percent. *E.g.*, 88-1250 Pet. 6, 7, 15-16. As noted above (note 6, *supra*), AT & T's authorized rate of return during the first two months of 1976 was only 8.5 percent. Because AT & T was not authorized to earn 9.5 percent throughout 1976, its failure to achieve a 9.5 percent return in 1976 does not establish a shortfall.

In any event, AT & T had an opportunity to earn the prescribed level (plus the margin) by filing rates and conducting its business. Customers, by contrast, had no choice but to pay the tariffed rates. It is hardly unfair to a carrier, even if a shortfall were shown, to disallow a second opportunity to achieve the prescribed level of earnings. See *FPC* v. *Tennessee Gas Transmission Co.*, 371 U.S. at 153, 150-155 (company must shoulder hazards incident to its action in filing rates, "including not only the refund of any illegal gain but also its losses where its filed rate is found to be inadequate").

and to lower its prescribed ceiling to the level justified by current conditions.[18]

Finally, the provisions of the statute are not perfectly symmetrical; indeed, they embody a distinction between carriers and ratepayers that the refund order of the Commission reflects. Pet. App. 14a. Thus, while carriers propose their own rates, and may seek increases when appropriate, ratepayers do not have a comparable power of initiation: they must generally rely on the Commission itself for protection. The refund order assists in that protection. Indeed, the Commission's order is entirely in keeping with the provisions of the statutory scheme that expressly permit recovery from a carrier for violations of a duty under the Act. *E.g.*, 47 U.S.C. 204, 206-209. In short, requiring AT & T to refund earnings it received in violation of outstanding prescription orders did not disturb the statutory balance of interests, but rather vindicated that balance.[19]

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[18] The Commission in 1981 prescribed a rate of return for AT & T of 12.75 percent, with a buffer of .25 percent. *AT & T*, 86 F.C.C.2d 221 (1981), aff'd, *United States* v. *FCC*, 707 F.2d 610 (D.C. Cir. 1983). Subsequently, economic circumstances changed significantly in a direction indicating that the rate of return (and thus the rates) should be lower. AT & T, however, was permitted to earn a rate of return of 13 percent under the 1981 prescription order until the FCC superseded that order with a new one. The Commission did not do so until 1986. *Authorized Rates of Return for the Interstate Services of AT&T Communications and Exchange Telephone Carriers* (CC Docket No. 84-800 Phase III), FCC 86-354 (released Aug. 25, 1986).

[19] Judge Starr, in his concurrence in the case concerning the Commission's general rulemaking on refunds, argued (Pet. App. 157a-158a) that the 1933 amendment of Section 15a of the Interstate Commerce Act (ICA), just prior to Congress's enactment of the Communications Act of 1934, shows that recapture of recoveries in excess of a prescribed rate of return is inconsistent with congressional intent behind the 1934 Act. But, even aside from the danger of relying heavily on a different statutory scheme for an industry with a different

2. The court of appeals' holding affirming the Commission's refund order in this particular case is also correct on a ground not adopted by the court of appeals. Petitioners acknowledge, as Section 204 expressly states, that the Commission has authority to require carrier refunds of excess charges if those charges were suspended, allowed to take effect pending an investigation, and subjected to an accounting order. 88-1249 Pet. 4; 88-1250 Pet. 13 n.19, 16. Contrary to petitioners' suggestion, however (see note 5, *supra*), that is precisely what the Commission did with respect to the AT & T rates that are at issue in this case. Accordingly, Section 204 (in conjunction with Section 4(i)) independently supports the Commission's refund order and the court of appeals' judgment. While this Court's review of the court of appeals' holding is not for that reason precluded, the existence of an independent ground supporting the judgment counsels against review.

a. The rates that resulted in excessive revenues in 1978 were set forth in tariff revisions filed by AT & T on Jan-

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history and different problems, the ICA amendment does not have the suggested significance. The provision that Congress replaced (a) established a single fair rate of return for all railroads in the country or in a particular designated group, based on the aggregate value of those railroads' property, and (b) required each railroad then to place into certain contingency reserves any earnings that exceeded that rate of return, regardless of the railroad's individual circumstance. See 41 Stat. 488-491. The provision did not set a carrier-specific rate of return and then require disgorgement of earnings that exceeded that rate. The House Report (H.R. Rep. No. 193, 73d Cong., 1st Sess. 27-30 (1933)), in explaining why the provision should be repealed, focused principally on the provision's grouping together of all railroads and the fluctuating conditions of individual railroads. Only one remark (quoted by Judge Starr (Pet. App. 158a)) concerns the incongruity of permitting carriers to earn more than they ought to earn and recapturing the excess, and that remark must be read in context, recognizing that the rate of return maximum at issue was not carrier-specific.

uary 19, 1976, to implement the Commission's rate of return prescription. *AT & T*, 58 F.C.C.2d 1. Exercising its authority under Section 204(a), the Commission suspended those tariff revisions for one day and set them for investigation. 58 F.C.C.2d at 4-5. The Commission required AT & T to "maintain an accounting of the revenues derived under these revised tariffs, for possible refund upon resolution of the lawfulness thereof." *Id.* at 4.[20]

The Commission had decided on the rate of return component of a just and reasonable rate, but it set for investigation numerous other issues that had to be resolved before the rate itself could be determined—*e.g.*, investments, cash expenses, and non-cash expenses. 58 F.C.C.2d at 4. Hence, as the order expressly noted, and contrary to petitioners' suggestions (see note 5, *supra*), the question whether the proposed rates actually would produce the fair rate of return that the Commission had prescribed was still open and part of the investigation. *Ibid.* The Commission cited Sections 204, 205, and 4(i) as sources of its authority to suspend, investigate, and require an accounting in this case. 58 F.C.C.2d at 5. The 1978 rates, therefore, were subject to refund under Section 204 to the extent they produced an actual rate of return that was unlawful (under the rate of return prescription) and, hence, was "not justified" (47 U.S.C. 204(a)).

The 1984 order directing the refund of such unjustified revenues was issued by the Commission while the 1976 accounting order, as well as various other accounting orders applicable to AT & T's 1978 rates, were still in effect. See Pet. App. 73a-85a (initial order, Appendix B). And, although the order directed the refund of the excess through a future rate reduction, it was a proper exercise of

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[20] See also Pet. App. 81a-93a (initial order, Appendix B) (pointing out that several other accounting orders with respect to AT & T's interstate services were in effect during 1978).

the Commission's Section 204 authority. Thus, the refund was "to the persons in whose behalf such amounts were paid" (47 U.S.C. 204), considered collectively—namely, to the (ever-changing) class of customers. Such an application of Section 204's refund authority is well within the Commission's Section 4(i) authority to make its powers effective, for as the Commission itself explained based in part on AT & T's comments (Pet. App. 53a-54a, 111a-112a), there would be insuperable obstacles to an individualized refund plan applicable to the customer base from years earlier. Plainly, Section 4(i) authorizes the Commission to give effect to Section 204's refund authorization without adopting a self-defeating plan that would waste a large part of the refund in administrative expenses (or a plan that imposed those expenses, in addition to the refund, on the carrier). Indeed, the accounting order imposed on AT & T itself required only class-wide accounting for this very reason (58 F.C.C.2d at 4-5)—and AT & T, of course, did not object—yet no individualized refund is possible based only on class-wide accounting.[21]

b. Although the court of appeals stated that Section 204 did not apply in this case (Pet. App. 12a), the court gave no explanation. For the reasons we have set out, the court's statement is incorrect: Section 204 supports the Commission's ruling in this case. And, although the Commission did not expressly rest its 1984 order on Section 204, there is no barrier to upholding the ruling on that basis.

Contrary to petitioners' suggestion (88-1250 Pet. 14 n.19), never in this proceeding has the Commission "disclaim[ed]" reliance on Section 204. Tellingly, peti-

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[21] Although large-scale refunds are rare, this is hardly a revolutionary refund mechanism in ratemaking. See, *e.g.*, *FPC* v. *Tennessee Gas Transmission Co.*, 371 U.S. at 154-155 & n.9; *Bebchick* v. *PUC*, 318 F.2d 187 (D.C. Cir.), cert. denied, 373 U.S. 913 (1963).

tioners cite no such disclaimer. Indeed, the Commission did not expressly claim exclusive reliance on Section 205 in conjunction with Section 4(i). See Pet. App. 59a. And the fact that the rates at issue were subject to an accounting order under Section 204 was repeatedly relied on at all stages of the present proceeding.

Thus, after AT & T had reported that its earnings in 1978 had exceeded a 10 percent rate of return, a petition by several citizens groups in July 1979 urged the Commission to require a refund, pointing out that AT & T's tariff filing had been subjected to an accounting order. See Pet. App. 40a n.1, 67a. The 1979 notice of inquiry that led to the refund order described the 1976 accounting order and noted that it had contemplated the possibility of refunds (75 F.C.C.2d at 415 & n.6), undertook to act on the citizens groups' petition for enforcement of the accounting order (*id.* at 414 n.5), and cited Section 204 as one of the statutory provisions that were relevant to its inquiry (75 F.C.C.2d at 416-417). In the 1984 order requiring petitioners to disgorge the excessive 1978 earnings, the Commission again referred to the citizens groups' petition for enforcement of the accounting order (Pet. App. 40a n.1) and explicitly granted that petition "to the extent stated in the rulings and procedures that have been adopted herein" (*id.* at 59a). In the same order, in rejecting the "retroactivity" argument that the rates at issue had previously become lawful, the Commission relied centrally on the fact that the 1978 rates had never been accepted as lawful, referring for elaboration to Appendix B, which explained that the rates were subject to numerous accounting orders, including the 1976 accounting order adopted under Section 204. *Id.* at 57a (referring to *id.* at 73a-85a (Appendix B)).[22]

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[22] The Commission stated in its reconsideration decision that it had not relied on "the accounting orders that are discussed in Appendix B of the *Restitution Decision* in formulating the restitution mechanism."

In its reconsideration order, the Commission again cited Appendix B in rejecting both the retroactivity argument and the argument that the rate of return prescription did not have binding effect. *Id.* at 102a n.55, 104a n.60.

In defending its order in the court of appeals, the Commission's brief did not expressly rely on Section 204. Nor did it disclaim reliance on that provision or claim exclusive reliance on Section 205.[23] At oral argument, moreover, the Commission, while acknowledging that this was not the agency's primary rationale for its action, contended "that the Commission did in fact exercise its section 204 powers here by suspending the rates, by setting up an accounting order, and that the accounting order remained valid in 1978 and that this is from that perspective a very traditional rate refund." Transcript of oral argument (Oct. 30, 1986), at 35-38.

In these circumstances, the refund order of the Commission may properly be upheld under Section 204 (in conjunction with Section 4(i)). To be sure, under *SEC* v. *Chenery Corp.*, 332 U.S. 194 (1947), a court may not uphold an agency ruling on any basis that was not relied on by the agency and that would require the court to substitute its own discretionary judgment for that of the agency. See *ICC* v. *Brotherhood of Locomotive*

Pet. App. 112a n.87. As we have noted, however (see note 7, *supra*), that statement merely explained why the Commission was adopting a discount in rates for the future instead of a customer refund plan based on the series of accounting orders described in Appendix B. It was not a disclaimer of reliance on Section 204.

[23] The brief (at 4-5 n.4) noted that the rates at issue were subject to an accounting order. It also stated (at 28), however, that "[i]f the Commission were to accept the position of the carriers in this case that it had no refund power except under Section 204 of the Act, the carriers would be free to ignore not just this rate of return prescription, but any prescription." To the extent that that statement overlooks the existence of a Section 204 accounting order in this case, it is mistaken.

Engineers, 107 S. Ct. 2360, 2368 (1987). But, in addition to the significant reliance actually placed on Section 204 by the Commission here, the *Chenery* principle does not preclude upholding the Commission refund order in this case under Section 204. If there is a valid statutory basis for an agency decision, the decision should be upheld on that basis—even if the agency relied on an incorrect statutory basis—if it is clear that the agency would have made exactly the same decision had it not relied on the incorrect statutory authority. See *Massachusetts Trustees* v. *United States,* 377 U.S. 235, 246-247 (1964). Here, it is beyond doubt that the Commission refund order would be the same under Section 204 or Section 205, and no discretionary element of the decision would be affected by which precise statutory basis supported the result. Plainly, the Commission would not abandon the objective of recouping AT & T's excessive 1978 earnings if it had to rely on Section 204, which does, after all, speak expressly of refunds. Accordingly, there is an alternative ground to support the court of appeals' judgment.

3. Even aside from the correctness of the court of appeals' holding and the existence of an alternative ground to support the judgment, this case does not merit review. First, the continuing significance of the question of refunds to enforce rate of return prescriptions is at present uncertain. The Commission recently adopted a system of "price caps" derived from current rates to replace the scheme of rate of return regulation for AT & T, and it has proposed a similar system for local exchange telephone companies. See FCC News Report No. DC-1379, *Commission Adopts Incentive Regulation for Dominant Carriers,* (Mar. 16, 1989). Such a system would eliminate or reduce substantially the Commission's primary reliance on rate of return prescriptions as a means of ratemaking, at least for AT & T. To that extent, it would effectively moot the refund issue.

If, on the other hand, the Commission pursues a policy of enforcing rate of return prescriptions through refunds (without a Section 204 accounting order), then there will be a better vehicle for reviewing that policy—one that does not involve a clear Section 204 basis for the policy. Indeed, the Commission is currently considering what steps to take on remand from the court of appeals' decision (Pet. App. 141a-159a) setting aside its general rule establishing procedures for the implementation of such a policy. If the Commission promulgates a new rule, a challenge to such a rule would provide a more suitable case for review of the refund question, as it would involve a more complete record on pertinent issues (such as the proper relation between rate of return excesses and shortfalls).

In short, although we believe that the refund issue, having been correctly resolved by the court of appeals, does not warrant this Court's review, there will be more appropriate occasions to review the question if it proves to be of continuing importance. Nor is there any equitable imperative for review of this particular case. In addition to the fact that the Section 204 accounting order put AT & T on ample notice of the possibility of a refund and independently supports the ruling, the present case merely involves the disgorgement of revenues that petitioners had no right to receive in the first place without violating the outstanding prescription order.

CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted.

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